

CREDIT OPINION

8 July 2019

Update

✓ Rate this Research

RATINGS

OBOS-banken AS

Domicile	Norway
Long Term CRR	A3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	Baa1
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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OBOS-banken AS

Update to credit analysis

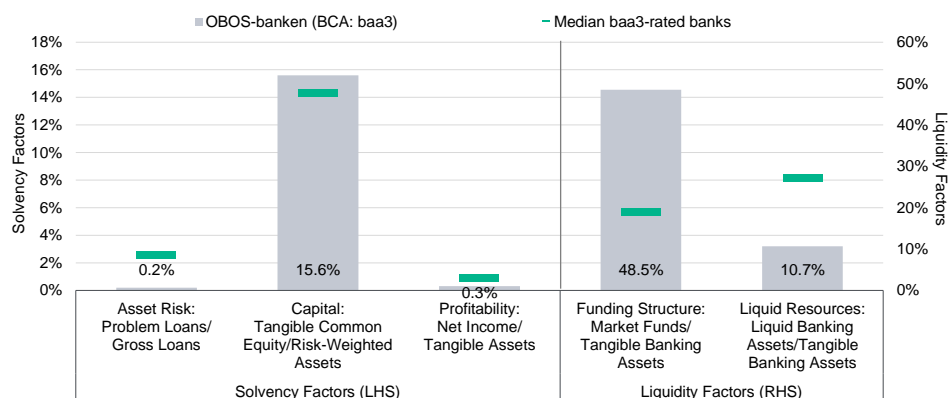
Summary

OBOS-banken AS's (OBOS-banken) Baa1 long-term deposit and issuer ratings are derived from (1) the bank's standalone creditworthiness reflected in its baa3 Baseline Credit Assessment (BCA); and (2) two notches of rating uplift from our Advanced Loss Given Failure (LGF) analysis that takes into account the risks faced by the different debt and deposit classes across the liability structure should the bank enter resolution.

The baa3 standalone BCA reflects the bank's: (1) strong asset quality aided by a relatively low risk housing mortgage-lending focus and a supportive operating environment; (2) adequate capital metrics, supported by capital injections from parent; (3) strong operating efficiency; and (4) comfortable liquidity position. These strengths are balanced against OBOS-banken's: (1) high geographical lending concentration, significant loan growth since inception, and its limited track record; (2) limited ability to raise capital outside the OBOS Group; (3) modest profitability and monoline business model; and (4) high reliance on wholesale funding.

Exhibit 1

Rating Scorecard - Key financial ratios



These represent our [Banks](#) methodology scorecard ratios. Asset risk and profitability reflect the weaker of either the three-year average and latest figure. Capital is the latest reported figure. Funding structure and liquid resources reflect the latest fiscal year-end figures.

Source: Moody's Financial Metrics

Credit Strengths

- » Strong asset quality and a supportive operating environment
- » Adequate capital metrics, supported by capital injections from parent
- » Very low loss-given-failure for deposits and senior unsecured debt

Credit Challenges

- » Modest profitability and monoline business model
- » Significant loan growth and concentration to the property market of Oslo and Akershus pose risks
- » High reliance on wholesale funding partially mitigated by sound liquidity position

Outlook

The outlook on the long-term deposit and issuer ratings is stable. The stable outlook reflects our forward looking view that OBOS-banken's profitability will remain relatively low over the next 12-18 months, while market funding will continue to be a major funding source despite deposit growth. The outlook also incorporates our expectation that asset quality will remain strong and capital metrics will rise along with higher capital requirements.

Factors that Could Lead to an Upgrade

- » Over time the bank's ratings may be upgraded as a result of: (1) a longer track record of strong asset quality and low loan losses, particularly through an entire economic cycle, along with a more moderate rate of loan growth and a seasoning of the bank's loan portfolio; (2) a sustainable improvement in profitability without an increase in the its risk profile; and/or (3) reduced reliance on market funding.
- » OBOS-banken's deposit and issuer ratings could also be upgraded in case the bank issues substantial amounts of more subordinated debt that would reduce the loss-given-failure of more senior creditors in a resolution scenario

Factors that Could Lead to a Downgrade

- » Downward pressure would develop on OBOS-banken's ratings because of: (1) unexpected deterioration in asset quality metrics, or, increase risk appetite such as a higher proportion of unsecured lending; (2) a sustained weakening in capital below the 0.5% buffer over capital requirements; or (3) reduced liquidity held on balance sheet.
- » The bank's deposit and issuer ratings could also be downgraded in case its liability structure changes in such a way that increases the expected loss-given-failure for these instrument. This could occur because of a higher proportion of covered bonds in favour of senior unsecured debt, and a lower amount of subordinated debt and low-trigger additional Tier 1 hybrid instruments.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moody's.com for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

OBOS-banken AS (Consolidated Financials) [1]

	03-19 ²	12-18 ²	12-17 ²	12-16 ²	12-15 ²	CAGR/Avg. ³
Total Assets (NOK Billion)	46.9	44.6	34.2	27.8	22.7	25.1 ⁴
Total Assets (USD Million)	5,448.9	5,144.9	4,182.2	3,231.3	2,560.5	26.2 ⁴
Tangible Common Equity (NOK Billion)	2.7	2.7	2.2	1.8	1.5	20.7 ⁴
Tangible Common Equity (USD Million)	315.3	309.1	273.5	209.9	166.3	21.8 ⁴
Problem Loans / Gross Loans (%)	0.2	0.2	0.3	0.2	0.4	0.3 ⁵
Tangible Common Equity / Risk Weighted Assets (%)	15.6	16.0	16.3	15.4	15.0	15.6 ⁶
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	3.4	2.4	3.8	3.0	5.1	3.6 ⁵
Net Interest Margin (%)	0.7	0.8	0.9	0.9	1.1	0.9 ⁵
PPI / Average RWA (%)	1.3	1.3	1.5	1.1	1.2	1.3 ⁶
Net Income / Tangible Assets (%)	0.3	0.3	0.4	0.3	0.3	0.3 ⁵
Cost / Income Ratio (%)	40.9	42.8	41.8	52.8	54.0	46.5 ⁵
Market Funds / Tangible Banking Assets (%)	35.5	48.5	41.5	41.6	42.6	42.0 ⁵
Liquid Banking Assets / Tangible Banking Assets (%)	14.5	10.7	15.3	13.6	12.7	13.4 ⁵
Gross Loans / Due to Customers (%)	221.5	230.4	187.8	169.7	175.4	197.0 ⁵

[1]All figures and ratios are adjusted using Moody's standard adjustments. [2]Basel III - fully-loaded or transitional phase-in; IFRS. [3]May include rounding differences due to scale of reported amounts. [4]Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime. [5]Simple average of periods presented for the latest accounting regime. [6]Simple average of Basel III periods presented.

Source: Moody's Investors Service; Company Filings

Profile

OBOS-banken is a Norwegian commercial bank mainly focused on retail mortgages and lending to housing companies (or cooperatives) in Norway. The bank reported total assets of NOK42.9 billion (equivalent to around €4.4 billion) as of March 2019.

OBOS-banken is part of the OBOS Group, one of the largest property developers in the Nordics. The bank is fully owned by OBOS Finans Holding AS, which in turn, is fully owned by OBOS BBL. Most of the bank's retail clients are either members or employees of the OBOS Group, while, in its wholesale business most customers are housing companies managed by OBOS Group.

OBOS Group's lending activities date back to 1929, however, OBOS-banken received its full banking license in 2013 and therefore its financial history is limited, while the bank also continues to develop its business and risk management profiles.

Detailed Credit Considerations

Strong asset quality, partly offset by significant loan growth and concentration to the property market of Oslo and Akershus

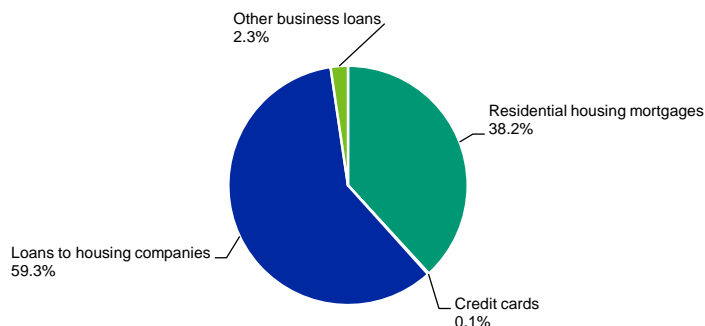
Our assessment of OBOS-banken's asset risk takes into account the bank's relatively low risk housing mortgage-lending focus within Norway's supportive environment, but also its high concentration in the areas of Oslo and Akershus and the Norwegian property market, significant loan growth since inception, and its limited track record as a bank-licensed institution.

OBOS-banken focuses on lower-risk secured retail and wholesale (housing companies) mortgages. The majority of the bank's on-balance-sheet lending portfolio is to housing companies, 59% as of year-end 2018 (see Exhibit 3), while direct residential mortgages made up most of the remaining loans at 38%. Based on the legal framework that governs housing cooperatives in Norway, members contribute a proportionate share of operating expenses, including debt servicing of the housing company, thereby reducing risk for the bank. However, the bank is exposed to the tail risk of a large property price decrease, a common feature among its local peers. This is because its sizeable mortgage exposure leads to a high concentration in Norway's property market, particularly in the Oslo and Akershus area where most of the bank's lending originates (around 80% of outstanding loans) and where property prices had increased rapidly in previous years.

The bank also entered the credit card sector in 2017 by offering its own credit cards to its members, as a way to further leverage its customer base and expand its product offering. Although we consider the unsecured consumer lending space risky, the relative size of this business remains low for OBOS-banken at around 0.1% of loans at the end of 2018.

Exhibit 3

OBOS-banken lends predominantly to housing companies and directly to individuals for residential mortgages On-balance-sheet loan book breakdown as of the end of 2018



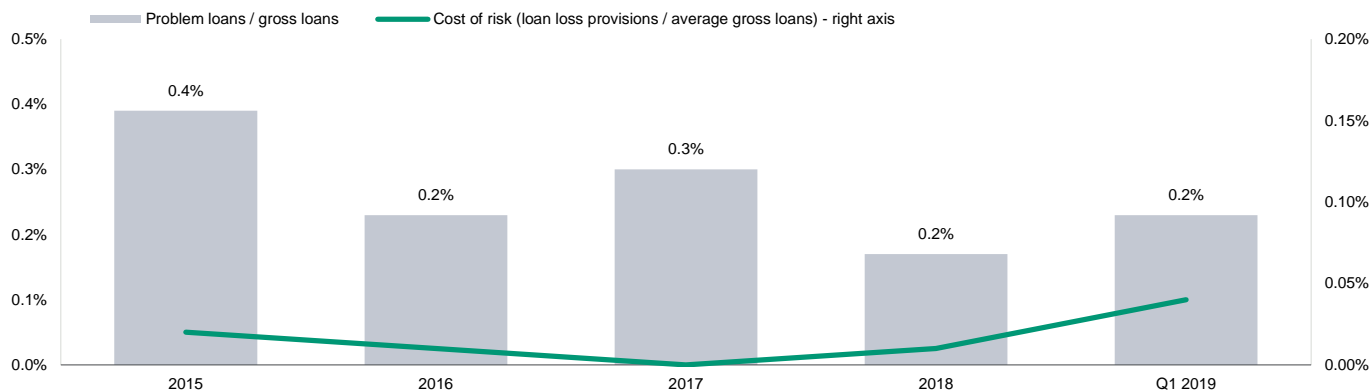
Note: OBOS-banken also transferred NOK4.4 billion of loans to housing companies to Eika Boligkreditt AS as of the end of 2018

Source: Company reports

We expect the repayment capacity of households in Norway to remain strong driven by low unemployment, real wage increases and a gradual increase in interest rates that will support the bank's asset quality.¹ In general, we consider the operating environment in Norway to be supportive, reflected in our '[Very Strong -](#)' macro profile. Therefore, we expect OBOS-banken's asset quality metrics to remain broadly unchanged over the next 12-18 months. The bank's problem loans ratio (IFRS 9 stage 3 loans as a percentage of total loans) remained low at 0.2% as of end-March 2019 (see Exhibit 4) and loan losses have been particularly low since the bank's inception.

Exhibit 4

OBOS-banken maintains very low credit costs thanks to a low problem loans ratio Asset quality metrics evolution



Source: Moody's Investors Service

Finally, our assessment also takes into account the limited seasoning of the bank's loan book and significant lending growth. The bank's loan book grew by a compound annual rate of 24% since its establishment in 2013, and by 19% in 2018 alone. Further, similarly to other recently established banks, OBOS-banken's performance through an entire economic cycle has not yet been demonstrated, which reduces the predictability of its performance, while the effectiveness of its underwriting standards and risk appetite has not been proven.

Adequate capital metrics, supported by capital injections from parent

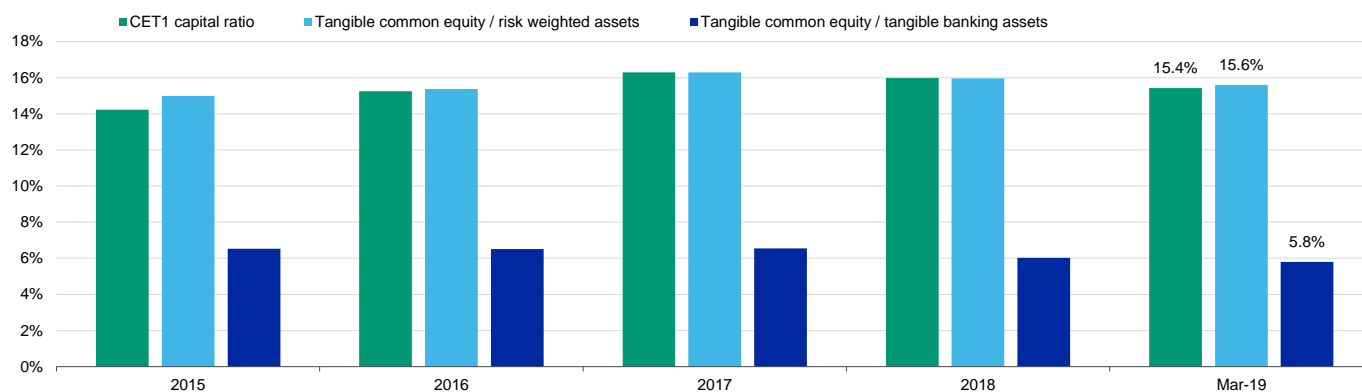
We view OBOS-banken's capital position as adequate and supported by regular capital injections by the OBOS Group along with earnings retention that enable its strong lending growth and allow the bank to maintain a margin above regulatory capital requirements.

OBOS-banken reported a common equity Tier 1 (CET1) capital ratio of 15.4% (see Exhibit 5) and a total capital ratio of 18.6% as of end-March 2019. These metrics were above a 14.7% CET1 regulatory requirement and an 18.2% total capital ratio requirement that applied for that period and that included a 3% systemic risk buffer and a 2% countercyclical capital buffer that applies for all banks in Norway, and a 2.7% pillar 2 requirement that is specific to OBOS-banken. Our capital measure, tangible common equity / risk-weighted assets was 15.6% as of end-2018. The countercyclical capital buffer will increase to 2.5% by the end of 2019, and the systemic risk buffer may [increase to 4.5%](#) by end-2021. We expect the bank's capital metrics will also rise to maintain an internal 0.5% buffer above regulatory requirements.

Exhibit 5

OBOS-banken's capital metrics remain adequate and above its regulatory requirements

Capital metrics evolution



Source: Moody's Investors Service

The bank's return on equity averaged a modest 5.9% during 2016-2018, which limited its internal capital generation capacity. Therefore, the bank has relied on capital injections from its parent to support its ambitious growth plans. We consider OBOS-banken to be central to OBOS Group's strategy and therefore we expect the group will continue to support the bank in its expansion plan. However, we also take into account that, given its sole ownership by the OBOS Group, OBOS-banken has fewer options to raise capital externally, in case of need, compared to peers.

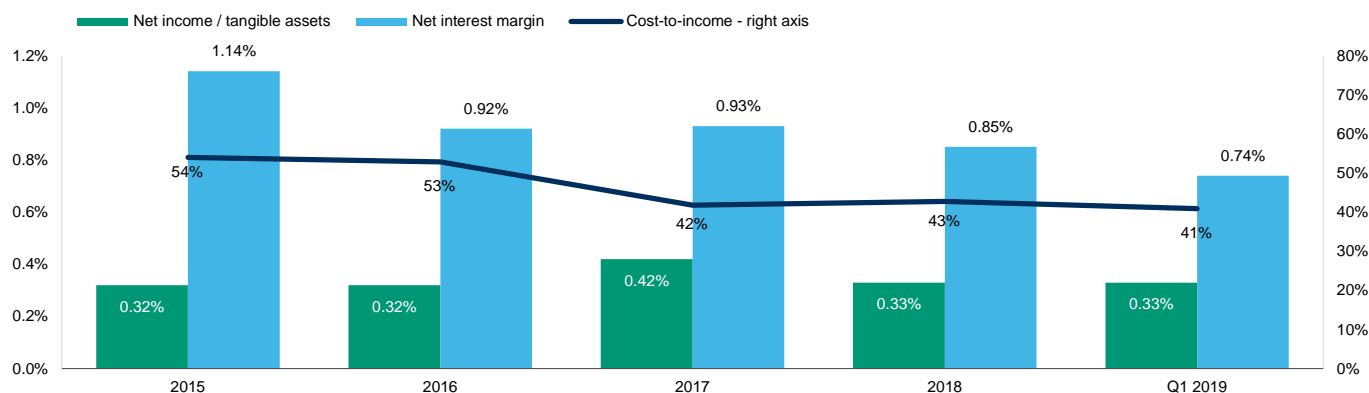
Modest profitability and monoline business model

Profitability is a relative weakness for OBOS-banken. However, we expect profitability will gradually improve along with greater economies of scale, widening net interest margins driven by interest rate hikes in Norway and continued focus on cost control.

OBOS-banken's net income relative to tangible assets (including off-balance sheet lending) was a modest 0.33% in 2018 and the first three months of 2019 (see Exhibit 6). However, cost-efficiency is relatively strong. The bank's cost-to-income ratio stood at 41% in the first quarter of 2019 and operating expenses accounted for 0.3% of total assets.

Exhibit 6

Profitability is relatively weak, although the bank is cost efficient OBOS-banken's profitability and efficiency metrics



Source: Moody's Investors Service

Similarly to other rated entities that are focused on one activity, we apply a one notch negative adjustment for a lack of business diversification to OBOS-banken's financial profile. This reflects that the bank's revenues are almost exclusively derived from its mortgage lending activities (both from individuals and housing companies).

High reliance on wholesale funding partially mitigated by sound liquidity position

OBOS-banken has a relatively high reliance on capital market funding, which would render it vulnerable to fluctuations in investor sentiment. As of end-March 2019, market funds accounted for 36% of tangible banking assets (including off-balance sheet covered bonds and assets). Market funding is primarily in the form of covered bonds and senior debt. The bank has a well-spread maturity profile, however, and has been issuing covered bonds directly through its subsidiary, OBOS Boligkreditt, since the end of 2016.

Going forward, we expect OBOS-banken to continue to focus more on customer deposits and covered bonds to fund lending growth.

The high reliance on market funding is mitigated by a sound liquidity position with liquid assets at 14.5% of tangible banking assets as of end-March 2019. Further, the bank reported a liquidity coverage ratio of 232%, well above the 100% regulatory requirement. The liquidity portfolio was primarily invested in covered bonds and other investment-grade rated bonds. However, we note that the covered bond holdings increase the interconnectedness between local banks and the domestic property market, a common feature among rated banks in Norway.

Source of facts and figures cited in this report's

Unless noted otherwise, the bank specific figures originate from bank's reports and Moody's Banking Financial Metrics. All figures are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to the document [Financial Statement Adjustments in the Analysis of Financial Institutions](#) published on 9 August 2018. The bank's figures are also adjusted to include loans transferred to [Eika Boligkreditt AS](#) (issuer rating Baa1 stable) that are not consolidated in OBOS-banken's financials, similar to our approach for other Norwegian banks that transfer mortgages to jointly-owned but not consolidated specialised companies.

Support and structural considerations

Loss Given Failure (LGF) analysis

Norway has transposed the EU Bank Recovery and Resolution Directive (BRRD) into local legislation in January 2019 and as such we consider the country an Operational Resolution Regime. In accordance with our methodology we, therefore, apply our Advanced LGF analysis, considering the risks faced by different debt and deposit classes - across the liability structure should the bank enter resolution.

In our Advanced LGF analysis for OBOS-banken, we use our standard assumptions and assume residual tangible common equity of 3% and losses post-failure of 8% of tangible banking assets. We also assume a 25% run-off of "junior" wholesale deposits and a 5% run-off in preferred deposits. Moreover, we assign a 25% probability to junior deposits being preferred to senior unsecured debt.

We also assume the proportion of deposits considered junior at 10% for OBOS-banken, relative to our standard assumption of 26%, because of the bank's largely retail-oriented deposit base.

Under these assumptions, our Advanced LGF analysis indicates that OBOS-banken's junior deposits and senior unsecured debt are likely to face very low loss-given-failure, due to the loss absorption provided predominantly by the volume of senior unsecured debt outstanding. This results in a two-notch rating uplift from the bank's BCA for both the deposit and issuer ratings.

Government support

Given the relatively small size of its operations, we believe there is a low probability of government support for OBOS-banken's deposits and senior unsecured debt, resulting in no rating uplift.

Counterparty Risk Rating

Counterparty Risk Ratings (CRRs) are opinions of the ability of entities to honour the uncollateralised portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honoured. CRRs are distinct from ratings assigned to senior unsecured debt instruments and from issuer ratings because they reflect that, in a resolution, CRR liabilities might benefit from preferential treatment compared with senior unsecured debt. Examples of CRR liabilities include the uncollateralised portion of payables arising from derivatives transactions and the uncollateralised portion of liabilities under sale and repurchase agreements.

OBOS-banken's CRR is positioned at A3/Prime-2

The CRR is positioned three notches above the Adjusted BCA of baa3, reflecting the extremely low loss-given-failure from the high volume of instruments that are subordinated to CRR liabilities.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails, and are distinct from debt and deposit ratings in that they (1) consider only the risk of default rather than both the likelihood of default and the expected financial loss suffered in the event of default, and (2) apply counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR Assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (for example, swaps), letters of credit, guarantees and liquidity facilities.

OBOS-banken's CR Assessment is positioned at A3(cr)/Prime-2(cr).

Similarly to the CRR, for OBOS-banken our Advanced LGF analysis indicates an extremely low loss-given-failure for the CR Assessment, leading to three notches of uplift from the bank's baa3 Adjusted BCA.

Methodology and scorecard

About Moody's Bank Scorecard

Our scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 7

OBOS-banken AS

Macro Factors

Weighted Macro Profile	Very Strong -	100%								
Factor	Historic Ratio	Macro Adjusted Score	Credit Trend	Assigned Score	Key driver #1	Key driver #2				
Solvency										
Asset Risk										
Problem Loans / Gross Loans	0.2%	aa1	↔	a2	Loan growth	Geographical concentration				
Capital										
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	15.6%	aa2	↔	a1	Access to capital					
Profitability										
Net Income / Tangible Assets	0.3%	ba2	↔	ba1	Expected trend	Earnings quality				
Combined Solvency Score		a1		a3						
Liquidity										
Funding Structure										
Market Funds / Tangible Banking Assets	48.5%	b1	↔	b1	Extent of market funding reliance					
Liquid Resources										
Liquid Banking Assets / Tangible Banking Assets	10.7%	baa3	↔	baa2	Stock of liquid assets					
Combined Liquidity Score		ba2		ba2						
Financial Profile										
Qualitative Adjustments										
				Adjustment						
Business Diversification				-1						
Opacity and Complexity				0						
Corporate Behavior				0						
Total Qualitative Adjustments				-1						
				Aaa						
Scorecard Calculated BCA range				baa2 - ba1						
Assigned BCA				baa3						
Affiliate Support notching				0						
Adjusted BCA				baa3						
Balance Sheet										
		In-scope (NOK Million)		% In-scope		At failure (NOK Million)		% At failure		
Other liabilities		21,607		46.1%		22,871		48.8%		
Deposits		18,055		38.5%		16,791		35.8%		
Preferred deposits		16,249		34.7%		15,437		32.9%		
Junior Deposits		1,805		3.9%		1,354		2.9%		
Senior unsecured bank debt		5,249		11.2%		5,249		11.2%		
Dated subordinated bank debt		350		0.7%		350		0.7%		
Preference shares (bank)		200		0.4%		200		0.4%		
Equity		1,406		3.0%		1,406		3.0%		
Total Tangible Banking Assets		46,867		100.0%		46,867		100.0%		
Debt Class										
		De jure waterfall		De facto waterfall		Notching		LGF	Assigned	Additional Preliminary
		Instrument	Sub-ordination	Instrument	Sub-ordination	De jure	De facto	Notching	LGF	notching
		volume +		volume +		vs.		Guidance	notching	Rating
		subordination		subordination		Adjusted		vs.		Assessment
		BCA								
Counterparty Risk Rating	18.3%	18.3%	18.3%	18.3%	3	3	3	3	0	a3
Counterparty Risk Assessment	18.3%	18.3%	18.3%	18.3%	3	3	3	3	0	a3(cr)
Deposits	18.3%	4.2%	18.3%	15.4%	2	3	2	2	0	baa1

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency rating	Foreign Currency rating
Counterparty Risk Rating	3	0	a3	0	A3	A3
Counterparty Risk Assessment	3	0	a3(cr)	0	A3(cr)	
Deposits	2	0	baa1	0	Baa1	Baa1

[1]Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

Ratings

Exhibit 8

Category	Moody's Rating
OBOS-BANKEN AS	
Outlook	Stable
Counterparty Risk Rating	A3/P-2
Bank Deposits	Baa1/P-2
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	A3(cr)/P-2(cr)
Issuer Rating	Baa1
ST Issuer Rating	P-2

Source: Moody's Investors Service

Endnotes

1 For trends in unemployment and real wage growth see also [Government of Norway – Aaa stable - Annual credit analysis](#), 28 June 2019

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